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STATEMENT OF  
HENRY ESCHWEGE, DIRECTOR  
COMMUNITY AND ECONOMIC DEVELOPMENT DIVISION  
BEFORE THE SUBCOMMITTEE ON CONSERVATION AND CREDIT <sup>00/01</sup>  
OF THE  
COMMITTEE ON AGRICULTURE ~~00/00~~  
HOUSE OF REPRESENTATIVES  
ON  
[ FARMERS HOME ADMINISTRATION'S ECONOMIC EMERGENCY  
LOAN PROGRAM ]

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MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

WE ARE HERE AT YOUR REQUEST TO DISCUSS OUR CURRENT RE-  
VIEW OF THE FARMERS HOME ADMINISTRATION'S (FMHA'S) ECONOMIC  
EMERGENCY LOAN PROGRAM. THE REVIEW IS NOT YET COMPLETED, BUT  
IN VIEW OF YOUR PENDING DECISION ON THE FUTURE OF THE PROGRAM,  
WE ARE GLAD TO PROVIDE YOU SOME OF OUR TENTATIVE FINDINGS  
AND OBSERVATIONS.

BACKGROUND

THE ECONOMIC EMERGENCY LOAN PROGRAM STARTED ON AUGUST 4,  
1978, AND IS SCHEDULED TO TERMINATE MAY 15, 1980. LOANS ARE  
TO BE MADE TO FARMERS AND RANCHERS WHO HAVE A REASONABLE PROS-  
PECT FOR SUCCESS WITH THE ASSISTANCE OF A LOAN AND WHO NEED  
THE CREDIT TO MAINTAIN A VIABLE OPERATION. BORROWERS MAY BE  
ELIGIBLE IF THEY CANNOT GET CREDIT AT REASONABLE RATES AND  
TERMS FROM NORMAL CREDIT SOURCES DUE TO NATIONAL OR AREAWIDE  
ECONOMIC STRESSES OR, UNFAVORABLE RELATIONSHIPS BETWEEN COSTS

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AND PRICES. THE TOTAL PRINCIPAL BALANCE OUTSTANDING AT ANY ONE TIME ON INSURED AND GUARANTEED LOANS CANNOT EXCEED \$4 BILLION.

THE FmHA INSURED AND GUARANTEED LOANS ARE MADE FROM OR GUARANTEED BY THE ECONOMIC EMERGENCY LOAN FUND (A REVOLVING FUND) AND BOTH ARE INSURED THROUGH THE AGRICULTURAL CREDIT INSURANCE FUND. INTEREST RATES FOR THE INSURED LOANS, WHICH IN EFFECT ARE DIRECT LOANS, ARE BASED ON THE COST OF GOVERNMENT BORROWING. CURRENTLY, THE INTEREST RATE ON REAL ESTATE-SECURED LOANS IS 10 PERCENT; AND ON CHATTEL-SECURED LOANS, 10.5 PERCENT. THE INTEREST RATE FOR GUARANTEED LOANS IS NEGOTIATED BY THE BORROWER AND THE LENDER.

ECONOMIC EMERGENCY LOANS CANNOT BE USED TO PURCHASE OR LEASE ADDITIONAL LAND. THE TOTAL AMOUNT OF LOANS AT ANY TIME FOR A BORROWER CANNOT EXCEED \$400,000 AND CAN BE USED TO REFINANCE EXISTING DEBTS; REORGANIZE OPERATIONS; PURCHASE OPERATING SUPPLIES, STOCK, AND EQUIPMENT; AND PAY OTHER ESSENTIAL OPERATING EXPENSES. AT JANUARY 19, 1980, FmHA HAD APPROVED AND OBLIGATED ABOUT \$3.9 BILLION AND HAD RECEIVED REPAYMENTS OF ABOUT \$243 MILLION; THEREFORE, ALMOST \$366 MILLION WAS STILL AVAILABLE FOR LOANS BEFORE THE PROGRAM EXPIRES IN MAY 1980.

#### RESULTS OF REVIEW

OUR REVIEW OBJECTIVE WAS TO EVALUATE THE EFFECTIVENESS OF THE PROGRAM AND WAS PRIMARILY DIRECTED TOWARDS ANALYZING A CROSS-SECTION OF ECONOMIC EMERGENCY LOAN FILES IN 10 STATES

WITH HIGH DOLLAR VOLUME, HIGH LOAN VOLUME, HIGH AVERAGE SIZE LOAN AMOUNT, AND A COVERAGE OF DIFFERENT TYPES OF FARM OPERATIONS. IN EACH STATE, WE SYSTEMATICALLY SAMPLED LOAN FILES TO DETERMINE (1) THE FINANCIAL STATUS OF THE BORROWERS, (2) THE AVERAGE LOAN SIZE AND TERM, (3) HOW THE LOAN PROCEEDS WERE USED, AND (4) THE EXTENT TO WHICH THE BORROWERS COULD HAVE OBTAINED CREDIT FROM NORMAL SOURCES. IN TOTAL, WE EXAMINED 101 LOAN FILES OUT OF A UNIVERSE OF ABOUT 19,400 IN THE 10 STATES. THE 101 LOAN FILES INCLUDED INDIVIDUAL FARMERS, PARTNERSHIPS, AND FAMILY CORPORATIONS. WHILE THE SAMPLE CANNOT BE PROJECTED TO THE UNIVERSE, WE FOUND NO EVIDENCE OF THESE LOAN FILES BEING ATYPICAL.

OUR ANALYSIS SHOWED THAT THE AVERAGE BORROWER OF AN ECONOMIC EMERGENCY LOAN HAD A NET WORTH OF \$202,000 AND A FARM OF ABOUT 570 ACRES. THE AVERAGE LOAN WAS ABOUT \$137,000 AND WAS REPAYABLE FOR PERIODS UP TO 40 YEARS. SOME LOANS WERE MADE TO COVER CURRENT OPERATING COSTS AND WERE PAYABLE WITHIN A YEAR, BUT MOST WERE FOR 7- TO 40-YEAR PERIODS AND WERE SECURED BY EQUIPMENT AND CROP CHATTELS OR REAL ESTATE MORTGAGES. THE MAIN PURPOSE OF THE LOANS WAS TO INCREASE CURRENT CASH FLOW AND ASSIST WITH CURRENT OPERATIONS.

LET ME BRIEFLY DISCUSS SOME OF THE INFORMATION WE HAVE DEVELOPED.

GUARANTEED LOANS NOT  
POPULAR WITH LENDERS

ONLY ABOUT 4 PERCENT OF THE LOANS MADE AS OF SEPTEMBER 30, 1979, WERE GUARANTEED, WHILE 96 PERCENT WERE INSURED LOANS.

FmHA HAD GUARANTEED \$135 MILLION IN LOANS BUT HAD MADE \$2.95 BILLION IN INSURED LOANS. BEFORE THE PROGRAM GOT UNDERWAY, IT WAS ESTIMATED THAT 50 PERCENT OF THE LOANS WOULD BE GUARANTEED.

DISCUSSIONS WITH FmHA OFFICIALS AND BANKERS IN A WIDE RANGE OF COMMUNITIES INDICATED THAT

--BANKERS HAVE MADE NO COMMITMENTS TO PARTICIPATE IN THE GUARANTEED PROGRAM.

--BANKS ARE REFERRING BORROWERS TO FmHA SINCE THE BANKS GENERALLY PREFER TO HANDLE ONLY SHORT-TERM (1 YEAR) FARM OPERATING LOANS OR CONSUMER-TYPE LOANS AT HIGHER RATES AND SHORTER TERMS THAN THOSE USED BY FmHA.

IN ONE STATE WHERE GUARANTEED LOANS WERE BEING USED MORE EXTENSIVELY, WE FOUND THAT THIS OCCURRED BECAUSE THE FARMERS HAD MONTHLY INCOME FROM MILK CHECKS AND THEREFORE WERE PRESUMED TO BE ABLE TO MEET THE ESTABLISHED MONTHLY PAYMENTS. AS A PART OF THE GUARANTEED LOAN CONTRACT, THE LENDERS REQUIRED AN ASSIGNMENT OF A PORTION OF THE MONTHLY MILK RECEIPTS AS THE MONTHLY LOAN PAYMENT.

FmHA OFFICIALS AT BOTH THE STATE AND COUNTY LEVELS HAVE STATED THAT THE ECONOMIC EMERGENCY LOAN PROGRAM "BAILED OUT" THE BANKS AND DID VERY LITTLE TO ENCOURAGE LENDERS TO PARTICIPATE IN FARMING LOANS. FmHA HAS NOT BEEN AGGRESSIVE IN PUBLICIZING AND PROMOTING THE GUARANTEED PORTION OF THE PROGRAM.

ECONOMIC EMERGENCY LOAN FUNDS  
USED IN LIEU OF OTHER PROGRAM FUNDS

ECONOMIC EMERGENCY LOAN FUNDS WERE USED IN LIEU OF FARM OWNERSHIP AND FARM OPERATING LOANS. FmHA OFFICIALS CONSIDER THE ECONOMIC EMERGENCY LOAN PROGRAM A GOOD SUPPLEMENT TO THE OTHER FmHA PROGRAMS AND BELIEVE IT SHOULD BE CONTINUED BECAUSE OF ITS BENEFIT TO THE FARMERS. THESE OFFICIALS CONTEND THIS IS SO BECAUSE THE FUNDING ON FARM OWNERSHIP AND OPERATING PROGRAMS IS OFTEN EXHAUSTED. ALSO, UNLIKE THE ECONOMIC EMERGENCY LOAN PROGRAM WHICH ALLOWS LOANS TO BE MADE UP TO \$400,000 PER BORROWER, AN INSURED LOAN UNDER THE FARM OWNERSHIP PROGRAM IS LIMITED TO \$200,000, AND AN INSURED LOAN UNDER THE OPERATING LOAN PROGRAM IS LIMITED TO \$100,000.

INFORMATION OBTAINED IN EACH COUNTY VISITED INDICATED THAT ECONOMIC EMERGENCY LOANS WERE MADE BECAUSE REGULAR OWNERSHIP OR OPERATING LOAN FUNDS WERE LIMITED OR NOT AVAILABLE. THE FOLLOWING EXAMPLE SHOWS HOW THIS OCCURS. A RANCHER BORROWED \$386,000 OF WHICH \$167,500 WAS TO REFINANCE OLD DEBTS AND \$218,500 WAS FOR CURRENT EXPENSES AND TO PURCHASE LIVESTOCK. SINCE THE \$218,500 EXCEEDED THE MAXIMUM OF \$100,000 AVAILABLE UNDER THE OPERATING LOAN PROGRAM, FmHA MADE THE ENTIRE LOAN FROM THE ECONOMIC EMERGENCY PROGRAM.

A FURTHER EXAMPLE INVOLVES A FARMER WHO NEEDED \$15,000 FOR PRODUCTION EXPENSES AND \$4,000 FOR RENT ON LAND. HE QUALIFIED FOR AN OPERATING LOAN, BUT OPERATING LOAN FUNDS HAD BEEN EXHAUSTED SO HE WAS GIVEN AN ECONOMIC EMERGENCY LOAN.

REQUIREMENT THAT NO ADDITIONAL  
LAND BE PURCHASED OR LEASED IS  
CIRCUMVENTED

THE ACT PROVIDES THAT NO LOAN MAY BE MADE IF ITS PURPOSE IS TO PURCHASE OR LEASE ADDITIONAL LAND. ALTHOUGH WE FOUND NO DIRECT PURCHASE OR LEASING OF ADDITIONAL LAND WITH ECONOMIC EMERGENCY LOAN PROCEEDS, WE DID NOTE INSTANCES WHERE FARMERS HAD CONTRACTED TO BUY ADDITIONAL LAND ON SHORT-TERM DEMAND NOTES FROM THEIR BANKS IMMEDIATELY PRIOR TO APPLYING TO FmHA FOR AN ECONOMIC EMERGENCY LOAN TO COVER THE MORTGAGE. COUNTY SUPERVISORS TOLD US THAT SOME APPLICANTS QUALIFIED FOR A FARM OWNERSHIP LOAN, BUT SINCE NO MONEY WAS AVAILABLE IN THAT PROGRAM, ECONOMIC EMERGENCY LOANS WERE USED TO PAY BACK THE BANKS.

TESTS FOR CREDIT ELSEWHERE  
NOT UNIFORMLY APPLIED

THE ECONOMIC EMERGENCY LOAN PROGRAM WAS ESTABLISHED TO ALLOW FARMERS AND RANCHERS TO STAY IN BUSINESS WHEN THEY COULD NOT GET CREDIT AT REASONABLE RATES AND TERMS FROM NORMAL SOURCES DUE TO NATIONAL ECONOMIC STRESSES OR UNFAVORABLE RELATIONSHIPS BETWEEN COSTS AND PRICES. WE FOUND THAT ONLY IN ISOLATED CASES WERE TESTS MADE TO DETERMINE WHETHER CREDIT WAS AVAILABLE ELSEWHERE. FOR EXAMPLE, A FAMILY CORPORATION HAD ASSETS OF \$1,805,000 AND LIABILITIES OF \$377,000 RESULTING IN A NET WORTH OF \$1,428,000. THE FAMILY ONLY OWED \$104,000 AGAINST REAL ESTATE VALUED AT \$1,235,000. THE LOAN FILE INDICATED THIS TO BE A VERY WELL-RUN, VIABLE OPERATION. THE AMOUNT THE CORPORATION WANTED TO BORROW WAS GREATER THAN THE LOCAL BANK

WOULD LEND, BUT THE FmHA COUNTY SUPERVISOR SAID HE WAS REASONABLY SURE THE FEDERAL LAND BANK WOULD HAVE MADE THE LOAN. HOWEVER, THE CORPORATION PREFERRED NOT TO BORROW FROM THE FEDERAL LAND BANK; FmHA MADE THE LOAN FOR \$400,000.

REPAYMENTS OF EARLY  
INSTALLMENTS ARE DELINQUENT

THE PAY BACK ABILITY OF EARLY BORROWERS UNDER THE PROGRAM HAS NOT BEEN ESTABLISHED. WE FOUND INDICATIONS THAT DELINQUENCIES MAY BE A PROBLEM. ON JANUARY 8-10, 1980, WE RECONTACTED THE COUNTY OFFICES TO ASCERTAIN WHETHER THE PAYMENTS DUE ON JANUARY 1, 1980, HAD BEEN MADE. OUR TESTS ON THESE EARLY LOANS INDICATED THAT FOR 82 LOANS ON WHICH FIRST PAYMENTS WERE DUE, 38 PERCENT WERE DELINQUENT. FmHA HAD ANTICIPATED A DELINQUENCY RATE OF 15 PERCENT. IN TERMS OF DOLLAR DELINQUENCY, WE FOUND THAT 53 PERCENT OF THE DOLLAR PAYMENTS SCHEDULED WERE DELINQUENT.

ABILITY TO GRADUATE BORROWERS  
TO OTHER CREDIT SOURCES IS  
HIGHLY QUESTIONABLE

THE ACT PROVIDES THAT FOR INSURED LOANS THE APPLICANT SHOULD GRADUATE TO OTHER SOURCES SUCH AS BANKS AS SOON AS HE IS ABLE TO OBTAIN SUCH A LOAN. THE ECONOMIC EMERGENCY LOAN PROGRAM WAS TO KEEP THE BORROWER IN BUSINESS AND PROVIDE THE FARMERS THE OPPORTUNITY TO GET CREDIT FROM OTHER SOURCES.

OUR DISCUSSION WITH LENDERS, BORROWERS, AND FmHA OFFICIALS DISCLOSED THAT, GENERALLY, THE LENDERS WERE REFERRING BORROWERS TO FmHA FOR LONG-TERM LOANS. THE LENDERS PREFERRED

TO MAKE SHORT-TERM OPERATING LOANS AND HIGH RATE CONSUMER-TYPE LOANS FOR 1 TO 3 YEARS IN LIEU OF THE LONG-TERM, LOW RATE REAL ESTATE, AND OTHER CHATTEL LOANS FOR FARMERS. SINCE MOST OF THE LOANS ARE FOR LONGER TERMS AND BANKERS ARE NOT VERY INTERESTED IN THESE LOANS, THE ABILITY TO GRADUATE BORROWERS TO OTHER CREDIT SOURCES IS HIGHLY QUESTIONABLE.

#### OBSERVATIONS

THE RESULTS OF OUR REVIEW TO DATE SUGGEST THAT THE CONGRESS, IN CONSIDERING AN EXTENSION OF THE ECONOMIC EMERGENCY LOAN PROGRAM, MAY WANT TO

1. ENCOURAGE FmHA TO SEEK BANKS' PARTICIPATION IN GUARANTEED LOANS, ESPECIALLY WHEN SHORT-TERM LOANS ARE INVOLVED.
2. DECIDE WHETHER IT WISHES TO CONTINUE HAVING THE ECONOMIC EMERGENCY LOAN PROGRAM BE, IN EFFECT, A SUPPLEMENT OF THE EXISTING FARM OWNERSHIP AND OPERATING LOAN PROGRAMS. ALTERNATIVES MIGHT BE TO (1) RAISE THE LIMITS ON THE FARM OWNERSHIP AND OPERATING LOAN PROGRAMS AND TERMINATE THE ECONOMIC EMERGENCY LOAN PROGRAM AND (2) HAVE ONE COMBINED PROGRAM TO COVER THE PURPOSES OF THE PRESENT FmHA FARMER LOAN PROGRAMS.
3. EXPRESS ITSELF ON WHETHER IT WANTS TO PRECLUDE THE REFINANCING, WITH ECONOMIC EMERGENCY LOAN FUNDS, OF ADDITIONAL LAND ACQUISITIONS AND LEASES INITIALLY FINANCED BY BANKS ON A SHORT-TERM BASIS TO CIRCUMVENT

THE ACT'S PROHIBITION AGAINST SUCH FINANCING. FOR  
EXAMPLE, THE CONGRESS MAY WANT TO SET A TIME LIMIT  
ON HOW LONG PROPERTY MUST BE OWNED BEFORE IT CAN  
BE REFINANCED WITH ECONOMIC EMERGENCY LOAN FUNDS.

4. REEXAMINE THE POSSIBILITY OF TIGHTENING THE CREDIT  
ELSEWHERE PROVISIONS OF THE ACT TO BRING THEM IN  
LINE WITH PROVISIONS OF THE FARM OWNERSHIP AND  
OPERATING LOAN PROGRAM REQUIREMENTS.
5. KEEP APPRISED OF DELINQUENCY RATES AND GRADUATIONS  
EXPERIENCED AND PROVIDE FOR A REEXAMINATION OF  
PROGRAM EXPERIENCE WITHIN A YEAR.

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THIS CONCLUDES MY PREPARED STATEMENT, MR. CHAIRMAN.  
WE WILL BE PLEASED TO RESPOND TO YOUR QUESTIONS.